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TAGS: [ECON](#) [IS](#) [LE](#) [PGOV](#)

SUBJECT: LEBANON: ECONOMY IS "FINE FOR NOW," BUT RISK
LOOMS AS GOL DITHERS

Classified By: Classified By: Jeffrey Feltman, Ambassador, per 1.4 (b)
and (d).

Summary

11. (C/NF) Lebanese Minister of Finance Jihad Azour describes Lebanon's economy and financial situation as stable in the short run, but in need of stability and reinvestment for long-term viability. Azour showed little hope that projected record revenues for the Lebanese tourism and export sectors would recover. Confirming Embassy perceptions, Azour said that reconstruction coordination within the GOL was almost nonexistent, with each administration left to make its own assessments. On donor coordination, Azour outlined his plans to organize Lebanon's foreign and domestic aid donations into reconstruction funds similar to those used by the UN in Sudan and Iraq. On Hizballah, Azour brushed aside concerns of Hizballah money controlling the reconstruction efforts, but blanched at the possibility of confronting the party on arms smuggling. Azour also predicted that ongoing Israeli threats on Hizballah party members could be used as a further excuse for maintaining Hizballah's arms. End Summary.

LEBANESE ECONOMY STRONG...FOR NOW

12. (C/NF) In two separate meetings with Ambassador and emboff on August 18 and August 21, Minister of Finance Jihad Azour highlighted the relative financial health of the Lebanese economy. Azour characterized the monetary and public finance situation as "under control," noting that the pressure on the GOL was "less acute than in 2005" (after the Hariri assassination). Azour credits this stability to the USD 1.5 billion in deposits from the Saudis and Kuwaitis to the Central Bank, along with previous financial measures taken by his administration that allowed additional flexibility for the GOL without the need for additional liquidity.

13. (C/NF) According to Azour, the Treasury was already running with a high level of liquidity prior to the start of the conflict, thus allowing the GOL to maintain its payroll and other expenditures without resorting to additional borrowing. Payments on GOL public debt continued during the crisis and could continue for the next six months, said

Azour, even should there be no improvement in the economic situation.

14. (C/NF) Azour lamented that the conflict with Israel torpedoed what was shaping up to be a record year for Lebanon's economy. The Finance Ministry estimates that the first six months of 2006 produced a USD 850 million primary surplus in revenues, an amount five times higher than the same period last year. Based on the same six-month performance, Lebanese exporters estimated USD 2.5 billion in exports by year's end. While exports on track to account for over 30 percent of Lebanon's GDP for 2006 prior to July 12, Azour worries that the conflict will cause Lebanon's business leaders to remove their capital from Lebanon's volatile markets.

"BUSINESS AS USUAL" ATTITUDE NEEDED

15. (C/NF) Looking ahead to the near future, Azour stressed that the GOL needs to take steps to refuel growth in Lebanon's economy. "Pressure on public finance is happening now," emphasized Azour. Noting a fundamental lack of confidence among investors, Azour admitted that many businesses that sustained direct and indirect losses in the conflict will rebuild, but not at the scale needed to keep Lebanon's economy booming. "They will not be bold in their investments," added Azour.

16. (C/NF) Azour expressed his desire to continue the affairs of his Ministry as "business as usual." Positive developments in the economy and the long-term viability of Lebanon hinge on larger macroeconomic reforms, he said.

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Azour estimates that the Treasury will lose an additional USD 700-800 million until the end of the year, between relief expenses and the cost of deployment of the LAF to the South, which Azour puts at USD 70 million USD. Azour expressed his concern that the GOL not "overspend" on construction, adding that the standard should be a return to "normalcy" for those affected, not "to build a mansion for everyone." Azour hopes that he can energize cooperation between the GOL and the private sector to bring about a new "national movement" to reform and re-create a stronger economy for Lebanon's future.

DONOR COORDINATION

17. (C/NF) Azour agreed with the Ambassador's criticism of the lack of coordination among GOL departments in setting universal government priorities for reconstruction and recovery. He explained that his responsibilities lie only in donor coordination and reconstruction as part of the Ministry's broader attempts at reform and re-activation of the economy. Azour admitted that he was "not the right person" to speak about the GOL's reconstruction priorities. He further clarified that each ministry had been charged with making its own assessment and list of priorities within its own sector. Azour described most of these reports as, "not valid enough to be quantified," citing wide variance between estimates.

18. (C/NF) Azour added that the GOL would need an independent international accounting firm to collate and validate any needs assessment. Azour admits that his Ministry needs technical assistance from the World Bank and the International Monetary Fund to help in the short-term (three months to two years) planning for Lebanon's recovery. He further suggested that any final report of Lebanon's reconstruction needs should come under the seal of the World Bank and perhaps the UNDP. "This would make it not just a (Lebanese) government exercise," concluded Azour, concerned about credibility and accountability.

¶9. (C/NF) According to Azour, PM Siniora was soon announce measures the GOL will take on solving housing issues for Lebanon's internally displaced persons (IDPs). The GOL has started with basic water system repair and other public works reconstruction. In addition, the Ministry of Education has already begun its plans for renovation of schools in the affected areas. The only difficulty Azour reports is that Hizballah does not give clearance for public works officials to enter Hizballah-controlled areas to make assessments and repairs.

¶10. (C/NF) Azour stated that he does not intend to travel to Sweden for an international donors conference organized by the GOS's Ministry of International Development later this month. Azour nonetheless has participated in several conference calls with the Swedes to, "give meaning to the meeting" by setting the terms for discussion and preliminary priorities. Azour questioned the timing of the conference, noting that the timeline seemed rushed to fit the Swedish PM's re-election campaign. Clearly unenthusiastic about the Sweden exercise, Azour was not optimistic about the outcome of the Stockholm conference due to the absence of an advance paper to discuss.

¶11. (C/NF) Azour plans to organize Lebanon's foreign and domestic aid donations into one or more reconstruction funds. These funds, set up according to internationally accepted models - such as those used by the UN in Iraq, Sudan, Bosnia and Kosovo - will include donor entities as part of the funds' governing apparatus. Azour plans to call on the GOL to establish a High Committee for Reconstruction in Lebanon, composed of highly visible Lebanese figures, to oversee a fully audited and transparent disbursement of reconstruction funds. Azour foresees the establishment of several funds - one fund for Arab donations, one for other international donations, and one for the Lebanese private sector.

EXCUSES FOR HIZBALLAH

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¶12. (C/NF) Turning to Hizballah, Azour offered that he was not concerned about Hizballah "throwing money around." For Azour, the message of Hizballah is more problematic than its spending habits. Hizballah is sending the wrong message to the outside world to encourage foreign investment. Azour is concerned that individuals will not be willing to invest if the probability of renewed conflict between Lebanon and Israel remains high. What concerns Azour is the perception of the GOL as an effete body. "An empowered government needs to be able to move and to be supported.... The state should win at least something," said Azour, referring to Shebaa Farms.

¶13. (C/NF) Azour considers the GOL's best opportunity to weaken Hizballah would be by removing Shebaa Farms as Hizballah's raison d'etre. That, coupled with the Lebanese Armed Forces' (LAF) deployment to the south, would "diminish Hizballah's ability to activate things internally." Azour dismissed the Ambassador's assertion that Hizballah might simply take up other territorial claims (i.e. the Seven Villages) as a pretext for its continued need to remain armed. Azour admitted that, after recent Israeli statements, even with a solution for Shebaa Farms, Hizballah would use the excuse of needing to protect Hizballah members from Israeli retaliation as an argument to maintain its arms.

¶14. (C/NF) Azour was reluctant to criticize the lack of GOL action on curbing arms smuggling into Lebanon. Even when confronted with the explicit concerns of the international community and Israel about arms smuggling and the explicit obligations on Lebanon under UNSCR 1701, Azour brushed off any plan to confront Hizballah. "Why is Israel focused on this?" asked Azour. "Accept that the country is divided on

Hizballah.... Politically, it doesn't work.... It's not the right time now."

¶15. (C/NF) Azour confirmed that he had met on August 20 with a delegation of Hizballah officials and MPs, including MP Muhammad Ra'ad. Azour confirmed that Ra'ad appeared to be in good health and uninjured, despite media speculation to the contrary. There recently had been much speculation as to Ra'ad's condition, given that he had not appeared in public in quite some time.

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